1933

Examination of May, 1933

Minnesota State Board of Accountancy

MINNESOTA STATE BOARD OF ACCOUNTANCY

EXAMINATION OF MAY, 1933

WEDNESDAY, MAY 17, 1933 — 8:30 A. M. to 10.00 A. M.

ORAL

10:00 A. M. to 12:00 M.

Economics and Public Finance

(Answer six questions.)

Question 1:

Define (*a*) value, (*b*) utility, (*c*) price, (*d*) wealth, (*e*) money.

Question 2:

One of the bills before Congress, intended to decrease unemployment, provides that except in industries involving perishable products including food and milk, five days of six hours each shall constitute a work-week. Outline the probable effects of such a measure on present economic conditions.

Question 3:

Reconcile the demand that the Government sponsor legislation which will provide more employment, with an equally insistent demand that the Government lessen its own expenditures so as to lighten the tax burden.

Question 4:

What is the economic effect resulting from such a pyramiding of corporate relationships as was brought out in the investigations of the Insull case?

Question 5:

Give reasons for and against the Federal Government establishing a national banking system under which deposits would be guaranteed, or "insured" as proposed by some.

Question 6:

What is the economic effect of price cutting when price cutting is practiced even to the extent of selling below cost?

MINNESOTA STATE BOARD OF ACCOUNTANCY

EXAMINATION OF MAY, 1933

WEDNESDAY, MAY 17, 1933 — 1:00 P. M. to 5:30 P. M.

Practical Accounting

Problem 1:

From the following information construct the net-worth section of the Lloyd Manufacturing Company's balance sheet at December 31, 1932:

(1) In February, 1927, when the corporation was established under the laws of the State of Delaware, it acquired all the net assets of the Lloyd Paper Box Company. The book value of the net assets to the transferor was $602,349.88, including goodwill of $100,000.00. Stock authorized and issued for these net assets consisted of 40,000 shares of non-voting no-par cumulative preferred having an annual dividend rate of 80 cents per share, payable on February 1, a stated value, as determined by the directors under the authority of the charter and by-laws, of $10.00 a share, and a redemption price of $12.00; and 20,000 shares of no-par common having a stated value of $5.00 per share. These shares were issued pro rata to the stockholders of the old company, 10 shares of preferred and 5 shares of common being exchanged for each outstanding $100-par-value share of the predecessor company. The excess paid-in value of $102,349.88 was credited to surplus.

(2) The subsequent history of the surplus account is as follows:

Balance of earned surplus at February 1, 1927, on books of Lloyd Paper Box Company		$202,349.88
Less—Portion capitalized on transfer to new company.		100,000.00
Balance appearing on books of new company		$102,349.88
Net Profit—		
1927 (February 1 — December 31)	$ 36,423.26	
1928	29,375.87	
1929	6,391.22	
1930	2,800.17	
1931	*112,647.90	
1932	*148,402.55	*186,059.93
Amount in excess of stated value received on sale, on July 1, 1929, of 20,000 shares of newly authorized no-par preferred at $11.00 per share		20,000.00
Transfer from capital stock accounts, authorized by		

Board of Directors, under provisions of charter and by-laws on July 1, 1932—	
Reduction in stated value of preferred to $6.00	240,000.00
Reduction in stated value of common to $1.00	80,000.00
Write-off of goodwill on July 31, 1932, authorized by Board of Directors	*100,000.00
Reduction in value of buildings and machinery to conform to new price levels, as reflected in report of National Appraisal Company as at July 31, 1932, as authorized by Board of Directors	*102,968.23
Additional 1932 provision for loss on 1928-30 accounts receivable arising from debtors adjudged bankrupt in 1932, although in previous years believed solvent	*49,650.37
Balance, December 31, 1932	$ 3,671.35

*Red.

(3) Among the assets at December 31, 1932, is an item of reacquired stock representing the repurchase for cash from the company's president on that date of 1,000 shares of common stock at $8.00 a share. It is expected that this stock will be resold during 1933.

Problem 2:

On May 4, 1933, you are called upon to prepare certain information preceding the liquidation of Employees Securities, Inc.

Employees Securities, Inc., was established November 1, 1930, with an authorized capital stock of 3,000 shares having a par value of $100.00 each. The purpose of the company was to enable the employees of the Pioneer Leather Company to acquire capital stock of the latter company by collective purchase on the open market. All the authorized stock was immediately subscribed for and payment was to be made at the uniform rate of two per cent down and two per cent on the fifth of each succeeding month. Unpaid subscriptions bore six per cent interest. No stock was to be issued until fully paid, except qualifying shares.

The first transaction of Employees Securities, Inc., was to purchase 1,000 shares of Pioneer's preferred stock at an average cost of $86.50 a share and 10,000 shares of Pioneer's common stock at an average cost of $19.25 a share. Funds were advanced for the purchase by Pioneer. On May 1, 1933, the market value of the preferred was $40.00 a share, and the common, $5.00 a share.

At the beginning of 1933 it became evident that owing to drastic cuts in the number of employees at the end of 1932 and in rates of compensation for those remaining, many subscribers already in arrears on their monthly installments would be unable to complete their subscription contracts. Accordingly, the subscribers, at a meeting held on April 29, 1933, gave the directors authority to liquidate the company in a manner most equitable for all concerned, with due regard for the subscribers who were in a position to continue their monthly installments. Under this authority, and the authority contained in a by-law providing for the cancellation of subscriptions the installments on which were four months in arrears, the Board decided to:

(1) Establish the equity of all subscribers at May 1, 1933;

(2) Liquidate subscriptions on which installments are unpaid four months or longer at May 1, 1933, on the basis of the amounts that should have been paid in on that date, but with no liability on the part of subscribers beyond the total sums actually paid in by them;

(3) Sell enough stock of the Pioneer Leather Company to provide for such liquidation;

(4) Permit and perhaps later require subscribers less than four months in arrears to complete their subscription contracts in full; and

(5) Dissolve the company by a distribution of the remaining net assets when the balance of the subscriptions has been paid.

Following is a trial balance of the company's books at the close of business on May 1, 1933:

	Dr.	Cr.
Cash in bank	$ 4,593.22	
Unpaid stock subscriptions	162,100.00	
Accrued interest	6,223.75	
Cost of incorporation	476.00	
Investment in Pioneer Leather Company, at cost—		
1,000 shares of 7% cumulative preferred	86,500.00	
11,000 shares no-par common	200,000.00	
Accounts payable now due		$ 224.99
Bank loan, due May 10, 1933		75,000.00
Capital stock		300,000.00
Surplus, May 1, 1932		5,134.43
Dividends received since May 1, 1932, from Pioneer Leather Company—		
Preferred		7,000.00
No-par-value common stock, at rate of $1.00		10,000.00
Stock dividend of 10% on no-par-value common stock, received September 1, 1932, valued at market as of date of declaration August 1, 1932		7,500.00
Interest received and accrued on unpaid stock subscriptions		11,235.35
Proceeds from life insurance policy on life of president		50,000.00
Interest paid through May 1, 1933, on bank loans	5,852.50	
General and administrative expenses	350.32	
Totals	$466,094.77	$466,094.77

Note that the liabilities do not include a provision for Federal income tax for the fiscal year ending May 1, 1933.

The tabulation below details the classes of subscriptions in arrears:

Number of Subscribers	Individual Amounts Subscribed for	Number of Monthly Installments in Arrears	Total Amounts in Arrears	Accrued Interest on Total Amount of Unpaid Subscriptions at May 1, 1933*
25	$ 200.00	12	$ 1,200.00	$ 150.00
10	200.00	18	720.00	100.00
5	200.00	6	120.00	15.00
5	200.00	4	80.00	20.00
40	250.00	18	3,600.00	425.50
8	250.00	6	240.00	6.00
42	500.00	8	3,360.00	440.25
10	500.00	4	400.00	40.00
20	1,000.00	15	6,000.00	629.50
10	1,000.00	5	1,000.00	50.00
8	3,000.00	6	2,880.00	320.00
6	10,000.00	10	11,000.00	1,500.00
2	10,000.00	4	2,600.00	175.75
1	20,000.00	6	2,400.00	349.50
Less than four months in arrears.....			6,500.00	2,002.25
			$42,100.00	$ 6,223.75

*Divisible equally among subscribers of each class.

You are asked to determine—

(1) The equity of the various classes of subscriptions at May 1, 1933.

(2) The immediate cash requirements of the company.

Problem 3:

From the information appearing below prepare a balance sheet of the Goldrox Company at December 31, 1932:

Cash in bank (less checks in payment of accounts payable of $19,572.27, dated December 31, 1932, but mailed to creditors January 5, 1933) .	$ 50,081.97
Petty cash (in which are included advances to employees of $575.00, which are to be repaid from next payroll)	1,000.00
Customers' notes (of which $15,419.50 past due are doubtful and believed to be but fifty per cent collectible)	82,064.48
Accounts receivable (including bad accounts of $18,672.27, doubtful items—fifty per cent collectible—of $39,961.59, and advances to officers of $10,500.00 for stock subscriptions and of $2,514.62 on open account)	137,111.56
Inventory of—	
Finished goods (including consignments received amounting to $3,095.56)	70,725.26
Work in process (excluding factory overhead of $4,604.71)	30,290.22
Raw material (merchandise in transit at December 31, 1932, not en-	

tered on books, $17,429.70)	56,977.43
Unexpired insurance premiums (in which are included the cash surrender values of $21,903.38 on officers' life insurance policies)	27,429.70
Bonds and stocks (market value of listed securities $132,055.21; unlisted stocks consist of investments at cost of $54,691.50 in affiliated companies)	194,412.93
Deposit with sinking fund trustee from which matured but unpresented bonds of $10,250.00 and unpresented interest coupons of $922.50 have been deducted	32,314.13
Unamortized bond discount and expense	4,604.71
Land	121,195.02
Building	444,467.18
Equipment, including equipment in use, fully depreciated, which cost $37,429.70	231,752.66
Patents, including worthless patents costing $11,903.38 on which accumulated amortization of $9,215.29 has accrued	132,810.48
Bank loan, on which interest of $815.00 has been prepaid, secured by bonds and stocks having a book value of $20,146.22	15,000.00
Subscriptions to stock in affiliated companies, payable January 1, 1934.	17,000.00
Trade accounts payable (included in which are debit balances totaling $9,859.31)	56,977.43
Estimated liability on contract for raw materials canceled December 20, 1932	9,200.00
Loan from stockholder secured by assignment of notes receivable of $22,316.19	20,000.00
Interest accrued on bonds	5,416.67
Other accrued expenses	23,978.16
6½% first mortgage bonds, payable $5,000.00 semi-annually on March 1, and September 1, to March 1, 1942, when balance matures	250,000.00
7% cumulative preferred stock authorized, par value $100.00	500,000.00
7% cumulative preferred stock unissued and unsubscribed	150,000.00
No-par common stock—2,000 shares authorized and issued, including 200 shares sold to officers on which the company has advanced $10,500.00	200,000.00
Surplus (before providing for depreciation reserves of $180,080.34, and reserve for amortization of patents of $110,907.10; but including surplus of $25,147.78 arising from revaluation of land)	669,665.47

MINNESOTA STATE BOARD OF ACCOUNTANCY

EXAMINATION, MAY, 1933

THURSDAY, MAY 18, 1933 — 8:30 A. M. to 12:00 M.

Practical Accounting

Problem 1:

Following is a trial balance, by total debits and credits, of the accounts of a joint venture known as "R and B Special," from which you are called upon to make certain analyses:

Account	Debit	Credit
Cash on hand	$118,717.48	$118,020.19
Brokers' receivables	83,568.02	65,339.15
Liberty bonds	32,316.16	32,698.33
Stocks	112,258.97	
Payable to brokers, etc.	72,572.40	116,144.38
3% sales tax	1,131.63	2,434.02
Paul Rady	1,085.78	17,500.00
E. R. Barnes	1,000.00	7,000.00
Stock sales		81,134.00
Interest received		680.00
Salaries	4,500.00	
Expenses	4,906.74	1,107.11
Totals	$432,057.18	$432,057.18

The trial balance, exactly as reproduced above, is in the handwriting of Arthur Bore, former bookkeeper, who has disappeared and taken with him or destroyed the books of account and all other records. Bore was in the employ of Paul Rady, a broker, and kept the books of the joint venture in addition to performing other duties in Mr. Rady's office. You are asked to determine from such meager information as is available whether it is possible that Bore, who was fully bonded, has appropriated any assets belonging to the venture. In addition to the trial balance, Mr. Rady has supplied you, mostly from memory, with the following information:

(*a*) The venture is about one year old and was formed between himself and E. R. Barnes, a former associate, for the purpose of speculating in the listed common stock of a certain corporation, the partners having contributed initial capital of $15,000.00 and $5,000.00, respectively. No compensation for personal services was to be allowed to either venturer. Profits were to be shared three-fourths and one-fourth, respectively. Fourteen thousand shares were purchased at different times and at different prices, the average price being somewhat in excess of $8.00 per share. Sales of 10,500 shares have been made at prices a trifle less than the purchase price. The balance of the shares is in Mr. Rady's possession and has a present market value of $9.00 per share; it is to be valued at average cost.

(*b*) There is a check on hand from a purchaser of stock amounting to $697.29. The drawee bank is, however, in the hands of a conservator.

(*c*) Accounts receivable from vendee brokers and accounts payable to vendor brokers upon circularization by Mr. Rady are found to agree with the balances indicated on the above trial balance.

(*d*) The Liberty bonds were purchased from excess funds at par plus accrued interest of $316.16, and have all been sold. Of the sales, bonds having a par value of $31,000.00 were disposed of at 102 plus accrued interest of $57.00; the remaining $1,000.00 bond was sold at 101 plus an uncertain amount of accrued interest, and the bookkeeper was accused shortly before his departure of having written off the bond and retained the proceeds from its sale. He insisted, however, that the proceeds had been properly accounted for.

(*e*) The sales tax was erroneously accrued by the bookkeeper, as a tax is payable to the State only on sales of so-called "tangible" personal property. Any sums already paid are recoverable from the State.

(*f*) A personal expense of Mr. Rady's amounting to $85.78 was properly transferred from expenses to his personal account. Each partner has withdrawn $1,000.00 in cash.

(*g*) The expenses of the venture, which according to the trial balance total about $3,800.00, were paid by Mr. Rady's brokerage firm and are apparently correct.

Prepare an analysis of the above trial balance and state whether any of the suspicions which have been directed against the bookkeeper may be correct.

Prepare also a tentative balance sheet and statement of operating results from the information that has been made available to you.

What further steps, if any, would you take to verify the report and figures you have submitted?

Problem 2:

The Vidette Manufacturing Company purchases in bulk a raw material which must be separated into thirteen grades before processing. Cost is prorated over these grades by the assignment to them of weights corresponding to their salability in the form of finished products. Grade K is weighted at

100; other grades are given weights corresponding to their relative value in production as compared with grade K.

A certain lot of the raw material was purchased for $3,638.45 and consisted of 737 items. The table following shows the grades into which the items fall, the factors assigned each grade and the quantity.

Grade	Factor	Quantity
A	40	25
B	45	100
C	50	125
D	55	50
E	60	75
F	65	30
G	70	43
H	75	75
I	80	75
J	90	30
K	100	42
L	110	38
M	115	29
		737

What cost should be assigned to each item in the various grades?

Problem 3:

From the information following, which you determine to be correct, prepare a consolidated balance sheet and statement of profit and loss:

Aetna Publishers, Inc., is an operating and holding company with two subsidiaries: one a printing company; the second, a jobber of paper and printing supplies, now on practically a non-operating basis because of the depression. The parent company markets several series of educational books turned out by its subsidiary and by other printing establishments. The parent company's trial balance follows:

AETNA PUBLISHERS, INC.

TRIAL BALANCE — DECEMBER 31, 1932

Cash in bank		$ 38,694.82	
Cash on hand		500.00	
Customers, all collectible		287,718.90	
Inventory at December 31, 1932, of books, all of which were acquired in 1932—			
Purchased from Playders Corp.	$ 48,238.50		
Other purchases	14,878.74	63,117.24	$ 63,117.24
Advances to—			
Playders Corp.		35,200.00	
Printers Supplies Company		171,280.58	
Investment in—			
Playders Corp., acquired on January 1, 1923:			

1,250 shares at cost of $110.00 per share.	137,500.00	
Printers Supplies Company, established in 1927 at cost of $82,000.00: 500 shares written down in 1932 to.	1,000.00	
Land { acquired January 1, 1930, from Playders Corp.; land at cost to transferor, building at then fair market value of $91,000.00 [net after depreciation] as determined by Acme Appraisal Co. }	10,000.00	
Building	150,000.00	
Reserve for depreciation.		72,500.00
Accounts payable.		68,284.43
Capital stock authorized and issued—6,000 shares		600,000.00
Earned surplus at January 1, 1932.		120,339.12
Sales		848,058.26
Rental income, which may be regarded as a fair apportionment to subsidiary companies of depreciation, taxes, and other *actual* costs.		3,600.00
Opening inventory (includes no items acquired from subsidiary companies)	36,847.11	
Purchases from Playders Corp.	580,723.31	
Other purchases.	65,499.62	
Selling and administrative costs, including depreciation of $4,500.00.	34,226.26	
Losses from bad debts, including stock write-down.	163,591.21	
Totals	$ 1,775,899.05	$ 1,775,899.05

The trial balance of Playders Corp. was:

PLAYDERS CORP.

TRIAL BALANCE — DECEMBER 31, 1932

Incompleted shop orders at December 31, 1932 (no purchases from Printers Supplies Company included) . . . .$	32,390.22	
Paper, ink and supplies at December 31, 1932, of which $28,800.00 represents paper acquired in 1932 from Printers Supplies Company.	82,319.12	$ 82,319.12
Machinery and equipment, at cost.	123,713.24	
Reserve for depreciation, unchanged since 1930. . .		123,713.24
Advances from parent company.		35,200.00
Capital stock 1,500 shares originally issued in 1915 at par		150,000.00
Paid-in surplus arising from retirement in 1920 of preferred stock at less than par.		34,525.00
Paid-in surplus from sale of building to Aetna Publishers, Inc., in 1930, at a price exceeding cost of $130,000.00 less accrued depreciation of $52,000.00		13,000.00
Deficit at January 1, 1932, of which $34,967.81 was accumulated prior to 1923.	176,087.99	
Sales to Aetna Publishers, Inc., at regular market prices		580,723.31

Paper purchased from Printers Supplies Company during 1932	138,624.33	
Inventory of raw materials and supplies at January 1, 1932, of which $6,320.33 represents paper acquired from Printers Supplies Company (no orders in process at this date)	54,728.13	
Shop rent paid Aetna Publishers, Inc.	3,000.00	
All other shop purchases and direct shop expenses incurred in 1932	408,617.64	
Totals	$ 1,019,480.67	$1,019,480.67

Only a few transactions appear on the books of Printers Supplies Company for 1932. Its trial balance follows:

PRINTERS SUPPLIES COMPANY

TRIAL BALANCE — DECEMBER 31, 1932

Cash in bank, representing checks drawn on bank account of Aetna Publishers, Inc.		$ 132.99
Customers, all collectible	$ 504.20	
Inventory at December 31, 1932, of paper, etc., at cost.	2,740.44	
Advances from parent company		171,280.58
Sales of similar items at similar prices to Playders Corp., at regular market prices; gross margin has remained unchanged during last several years		138,624.33
Sales to outside customers		4,438.23
Rental paid Aetna Publishers, Inc., for storage space	600.00	
All other direct costs of sales, including purchases of $85,764.38 and opening inventory of $2,312.50, less closing inventory of $2,740.44	94,775.04	
Officers' salaries	52,000.00	
Capital stock—500 shares authorized and issued		50,000.00
Paid-in surplus from assets contributed in excess of par value of stock		32,000.00
Earned surplus, January 1, 1932	245,856.45	
Totals	$396,476.13	$396,476.13

MINNESOTA STATE BOARD OF ACCOUNTANCY

EXAMINATION OF MAY, 1933

THURSDAY, MAY 18, 1933 — 1:00 P. M. to 5:00 P. M.

Accounting Theory

(Answer ten questions including No. 6 and No. 10.)

Question 1:

In discussing the collapse of the Insull companies, N. R. Danielian, writing in the April *Atlantic Monthly,* states: "It is a sad commentary on our corporation laws and on our accounting and auditing methods that we had to wait until a major depression descended on us to wake us up to see the real secrets of financial miracle-making . . . [Insull] manipulated accounts to the detriment of investors. This could be done . . . without apparently deviating from codes of accounting, because there is no standardization of accounting practice."

Do you believe this statement is true? Give reasons.

Question 2:

Distinguish between charges to surplus and charges to profit and loss—that is, when is it proper, if ever, to carry losses incurred or discovered during the year to unearned surplus or capital surplus?

Question 3:

The officials of a certain municipality each year issue a single balance sheet prepared by public accountants on which the one item of surplus shows a constant increase because of the capitalization of new buildings and equipment in amounts exceeding the annual allowance for depreciation. The leader of one faction in the city council insists that the method of accounting is faulty, that actually a deficit exists which is being added to every year. As proof he points to the fact that expenditures have exceeded available income for the last five years, and that during the same period the indebtedness of the city has nearly doubled. Explain how these apparently contradictory facts may be reconciled to each other. Have you any suggestions as to the manner in which the city's financial condition may be displayed more clearly?

Question 4:

The accounts of a State university contain no reserves for depreciation although full costs of all buildings and equipment appear on the records. Do you believe that depreciation reserves should be maintained? If so, how would you dispose of the annual provisions for depreciation?

Question 5:

What limitations must be considered in using cost data as a basis for establishing selling prices?

Question 6:

The Bertram Fixtures Corporation on October 1, 1929, purchased on contract a tract of vacant land adjoining its plant for $50,000.00, payable $10,000.00 in cash and $5,000.00 each year thereafter on October 1, with interest at 6%. The unpaid balance was secured by a first mortgage. Unpaid special assessments totalling $1,575.00 were assumed. General taxes for 1929 were to be pro rated.

On July 1, 1932, the board of directors, desiring to free itself of the burdensome contract and seeing no need for the land for some time to come, authorized the president to cancel the contract. On this date the books showed the following:

Vacant land—		
October 1, 1929	Original cost, including unpaid special assessments	$ 51,575.00
May 2, 1932	Special assessment for street lighting system	1,200.00
	General taxes for period from October 1, 1929, to June 30, 1932, paid or accrued	3,312.16
	Interest on unpaid balance from October 1, 1929, to June 30, 1932, paid or accrued	5,850.00
June 30, 1932	Total book value	$ 61,937.16

Liabilities at June 30, 1932—		
	Purchase money mortgage	$ 30,000.00
	Accrued interest to June 30, 1932	1,350.00
	General taxes accrued to June 30, 1932	600.00
	Unpaid special assessments	2,175.00
June 30, 1932	Total liabilities	$ 34,125.00

The vendor agreed to cancel the present contract and interest accrued thereon, assume unpaid taxes and assessments, and to give the company on option to repurchase for $35,000.00 on or before five years after July 1, 1932, upon the payment by the Bertram Corporation of $2,500.00. The president accepted the offer and paid the $2,500.00 on July 8, 1932.

On July 1, 1932, the property was appraised at $25,000.00.

Make the necessary entries as at July 1, 1932, to record this transaction. Give your comments.

Question 7:

A good many capital asset accounts have been written down during the past year. Under what conditions do you believe that such write-downs are proper?

Question 8:

Do you agree with a statement appearing recently in an annual report to stockholders that "no expense for depreciation can be said to have been incurred if such expense is not covered by operating income"?

Question 9:

Mr. J. M. B. Hoxsey, in a recent address to accountants, suggests, as an alternative to full depreciation write-offs during the period of the depression, that depreciation expense not chargeable to production be carried to an account to be known as "Deferred Depreciation Expense" which may be carried forward on the balance sheet and absorbed in succeeding prosperous periods. Comment on the suggestion.

Question 10:

In general, do you favor the practice followed recently by a number of industrial corporations of reversing in effect stock dividend entries made several years ago (and thus lowering stated value of outstanding shares) in order to restore capitalized earnings to surplus for the purpose of continuing dividend payments to stockholders?

Question 11:

Outline briefly the nature of the various kinds of surplus and how they should be set forth on a balance sheet.

Question 12:

Outline a number of methods by which a reserve for bad debts may be built up, and from time to time tested. What do you regard as the preferable method?

MINNESOTA STATE BOARD OF ACCOUNTANCY

EXAMINATION OF MAY, 1933

FRIDAY, MAY 19, 1933 — 8:30 A. M. to 12:00 M.

Auditing

(Answer ten questions including No. 8 and No. 9.)

Question 1:

In auditing the accounts of a village you find contracts for municipal improvements calling for expenditures greatly above the normal market price for such improvements. What action would you take in view of the fact that the village board which hired you to make the audit had approved all the contracts?

Question 2:

You find in auditing the accounts of the Banner Corporation for the year ending December 31, 1932, that instead of depositing with the trustee the $10,000.00 required to retire the serial bonds due on October 15, 1932, the check was issued to one of the three officers who acted as agent for all of them in acquiring from the bondholders the maturing bonds at the lowest price possible. The corporation then deposited the redeemed bonds with the trustee, the savings being retained by the officers. The three officers own all the outstanding stock.

What would be your attitude toward this transaction? How would you cover the point, if at all, in the balance sheet or certificate?

Question 3:

You have been called in by the president of a company to assist him in the drafting of a report to stockholders. He proposes to eliminate most of the comments preceding the financial statements because of unfavorable operating comparisons, and to draw the attention of stockholders to the strong cash position which has resulted from lowered receivables and inventories. In order that stockholders may be correctly informed, draft the comments you would add to the president's statement, assuming any facts conforming to the above general conditions.

Question 4:

Frequently in analyses of accounts receivable, items are disclosed which do not belong under the caption "Customers' Accounts." What are some of these items, and how would you classify them on the balance sheet?

Question 5:

In your examination of the opening and closing finished-goods inventory of a manufacturing company you find that at the end of 1931 the ratio of factory cost to expected selling price was 65%. At the end of 1932, because of lowered selling prices, lower production, and idle plant, the ratio has become 112%. What steps would you take in determining a better basis of inventory valuation for balance-sheet purposes?

Question 6:

Explain how obsolescence should be recognized and given expression to in the accounts of an automobile parts manufacturer.

Question 7:

In the past the two partners of the Booster Advertising Agency have had their personal bills paid through the firm checking account. During the past year were included such items as real estate and personal property taxes, Federal income taxes, prepayments and interest on first mortgages on their homes, in addition to ordinary withdrawals.

These facts are brought out during an examination of the partnership's records for a bank which desires certain information before making a loan. What emphasis would you give them in your report to the bank?

Question 8:

The president of a company has been in the habit of running the company's affairs under loose and inadequate by-laws, very much as he has seen fit, although in a number of instances he has subsequently sought the approval of the Board of Directors. As a business advisor you are asked, following an audit, to review certain of his acts in 1932 with the idea of recommending to the Board whether its authorization of these acts should precede or follow them. Outline briefly the procedure you would suggest in each case so that authority may be properly placed. The acts referred to were:

(1) Announcement of future declaration of dividends.
(2) Appointment of salesmanager who is to be compensated $50,000.00 per annum.
(3) Letting contract for construction of new plant in another city.
(4) Dismissal of company's secretary who is also an office employee.
(5) Preparation of annual report to stockholders.
(6) Repurchase of stock from dissatisfied stockholder at a premium.

(7) Accepting business requiring purchase of new machinery.
(8) Agreeing to additional assessment of Federal income tax liability.
(9) Starting patent infringement suit against competitor.
(10) Sale of unissued or treasury stock.

Question 9:

Outline in brief the general contents of a report covering a balance-sheet audit with which you are familiar and the style of which you approve.

Question 10:

Give the audit procedure you would follow in verifying a capital-stock account.

Question 11:

In a balance-sheet audit of a partnership what examination and verification would you make of the partners' drawing accounts?

Question 12:

Explain what you understand by Section 104 ("Accumulation of surplus to evade surtaxes") of the Federal Revenue Act of 1932. How would you determine whether evasion had occurred in any given case?

MINNESOTA STATE BOARD OF ACCOUNTANCY

EXAMINATION OF MAY, 1933

FRIDAY, MAY 19, 1933 — 1:00 P. M. to 5:00 P. M.

Commercial Law

CONTRACTS (Answer three).

Question 1:

(*a*) Differentiate between motive and consideration.
(*b*) Differentiate between good and valuable consideration.

Question 2:

What is the effect of an inadequate consideration for a contract?

Question 3:

A. & B. enter into a lease for a term of years with a clause in said lease providing for a renewal, without saying for what time and at what rent. At the end of the lease, B., the lessee, makes demand on A., the lessor, for a renewal of the lease. Can this contract be enforced?

Question 4:

Plaintiff delivers to the defendant a quantity of silk to be dyed, and when it was returned, it was found to be badly and unskilfully done. Plaintiff brought an action for the defective workmanship. The defense was that when the silk was delivered back to plaintiff, it was accompanied by a bill of charges on which was printed the notice, "all claims for deficiency or damages must be made within three days from date, otherwise not allowed," that plaintiff knew of such notice but made no claim within time; and that by accepting the goods, knowing of the notice, defendant claimed a contract was created on the terms of the notice. Is defendant's contention proper?

Question 5:

A, administrator of X, sold land to B under the belief that the administrator held a fee, both being of that opinion, whereas the administrator held nothing but an equity of redemption. Can this contract be enforced against the purchaser?

SALES (Answer three).

Question 1:

Define (*a*) sale, (*b*) conditional sale, (*c*) chattel mortgage.

Question 2:

(*a*) Define stoppage in transitu. (*b*) How may the right be exercised?

Question 3:

What are the implied warranties in sale by sample?

Question 4:

John Doe sends certain furniture chattels to the X Company, engaged in the furniture business, to be exposed for sale in the X Company's sales rooms where other similar articles belonging to the X Company are offered for sale. There is nothing on the articles belonging to John Doe to indicate any limitation on the right of the X Company to sell, and no public record affording constructive notice of any lien or title in John Doe. The X Company, without permission from John Doe, sells the property to Richard Roe. May Richard Roe retain the chattels as against the rights to John Doe?

Question 5:

A fraudulently induces X to sell him certain chattels. A sells the chattels to B in consideration of a pre-existing debt. X desires to reclaim the chattels because of the fraud of A. Can he succeed in retaking the property from B?

Question 6:

Give the distinction between delivery "on sale or return" and "consignment for sale."

CORPORATIONS (Answer four).

Question 1:

What is the trust fund doctrine as applied to the capital of a corporation represented by its capital stock?

Question 2:

A corporation is authorized to issue capital stock of a par value of $125,000.00. Finding itself in difficulty, it issues additional stock above its authorization in the sum of $25,000.00, on which a partial payment has been made. A receiver for the corporation having been appointed and the assets being insufficient to meet the claims of creditors, suit is instituted by the receiver against the new stockholders for the unpaid part of the capital stock. Can the receiver succeed?

Question 3:

What are right rights of a specific legatee of corporate stock as to dividends declared before and after the testator's death?

Question 4:

Define (*a*) corporation, (*b*) ultravires, (*c*) dividends as confined to corporation, (*d*) certificate of stock.

Question 5:

What is the distinction between De Jure and De Facto corporations?

PARTNERSHIP (Answer four).

Question 1:

A is a limited partner in X.Y.Z. On July 1, 1932, he withdraws as a partner, his capital being returned to him. At that time the partnership is solvent. On September 1, a receiver is appointed for the partnership which has become insolvent. At that time, there are a number of creditors who were such at the time of the withdrawal of the limited partner. What is the liability of the limited partner with respect to these creditors?

Question 2:

What is the extent of the property rights of a partner and the nature of the partner's right in specific partnership property?

Question 3:

Give the distinction between dissolution, termination and winding up of a partnership?

Question 4:

A. & B. are partners and agree to contribute capital of $8,000.00, divided equally between them. The partnership is in need of additional funds and B. advances the necessary money without an agreement among the partners as to interest. Is B. entitled to interest on his money in an accounting between the partners?

Question 5:

Define (*a*) partnership, (*b*) general partners, (*c*) ostensible partners, (*d*) nominal partners, (*e*) secret partners, (*f*) silent partners, (*g*) dormant partners, (*h*) special partners.

NEGOTIABLE INSTRUMENTS (Answer three).

Question 1:

John Doe, indebted to Richard Roe in the sum of $500.00, is adjudicated a bankrupt and receives his discharge. Subsequently, at the behest of Richard Roe, John Doe executes a new note in favor of the said Richard Roe. Should Richard Roe succeed in a suit for the collection of the note?

Question 2:

(*a*) Does a provision in a note for the giving of additional collateral destroy its negotiability?

(*b*) Does a provision in a note for giving collateral in the future prevent negotiability?

Question 3:

(*a*) What are the requirements of a negotiable instrument?

(*b*) Is the negotiability of a note destroyed that contains a provision providing that the note should be payable with cost of collection or attorney's fee in case payment shall not be made at maturity?

Question 4:

(*a*) Differentiate between special indorsement and indorsement in blank.

(*b*) Define restrictive indorsement; (*c*) qualified indorsement.

Question 5:

A negotiable note on which a corporation is an accomodation endorser finds its way into the hands of a holder in due course. After maturity, the note remaining unpaid is purchased by A. What defenses has the corporation against A in a suit on the note?

WILLS (Answer two).

Question 1:

Give the distinction between distribution Per Stirpes and Per Capita.

Question 2:

Define (*a*) last will and testament, (*b*) testator, (*c*) divisor, (*d*) devisee, (*e*) legatee.

Question 3:

Define (*a*) joint and mutual wills, (*b*) contingent wills, (*c*) holographic wills, (*d*) nuncupative wills.

Question 4:

(*a*) What is a codicil?

(*b*) What is the effect of the alteration of a will by a stranger?

BANKRUPTCY (Answer two).

Question 1:

What additional rights are lessors given by the new amendment to the bankruptcy act in cases of compositions by individuals?

Question 2:

(*a*) What is the time limit within which claims must be proved in bankruptcy?

(*b*) Which has priority of payment in bankruptcy: current wages due employees or federal taxes due to the United States Government?

Question 3:

The X Company issues its check on the National Bank & Trust Co., to John Doe, an employee, for wages earned. John Doe negotiates said check to the Wholesale Grocery Co. for cash, but before the check is cleared, the X Company is declared bankrupt. What preference, if any, is the Wholesale Grocery Co. entitled to, in the bankruptcy proceedings, as a holder of the check?

INCOME TAX (Answer two).

Question 1:

What, briefly, is the law with respect to the taxability of losses on corporate stocks and bonds held for less than two years, in the return of an individual?

Question 2:

Are losses on the sale of municipal bonds held less than two years deductible on the return of an individual?

AGENCY (Answer two).

Question 1:

A, gratuitously, undertakes to purchase certain property for his friend, B. Without disclosing the facts to B, A purchased the property for himself and resold it to B at an advanced price. Can B recover from A the secret profit made by him?

Question 2:

A, an infant, is appointed by X to sell certain chattels. Can X disaffirm the sale on the ground that his agent, A, is an infant?

Question 3:

Define: (*a*) agency, (*b*) principal, (*c*) agent.